IT IS ORDERED as set forth below:

Date: March 18, 2014

W. Homer Drake
U.S. Bankruptcy Court Judge

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF GEORGIA
NEWNAN DIVISION

IN THE MATTER OF:	:	**CASE NUMBER**
SYNERGY INVESTMENT GROUP, LLC	:	12-11609-WHD
Debtor.	:	
JAMES G. BAKER, Chapter 7 Trustee for the Estate of Envision LaGrange, LLC,	:	CONTESTED MATTER
Movant.	:	
v.	:	
TALON DN INVESTMENTS I, LLC,	:	IN PROCEEDINGS UNDER CHAPTER 11 OF THE BANKRUPTCY CODE
Respondent.	:	

ORDER

Before the Court is the Objection to Proof of Claim (hereinafter the "Objection")

of Talon DN Investments I, LLC (hereinafter "Talon"), filed by James G. Baker in his capacity as the Chapter 7 Trustee for the Estate of Envision LaGrange, LLC (hereinafter the "Estate"), a judgment creditor of the debtor, Synergy Investment Group, LLC (hereinafter "Synergy"). Talon opposes the Objection. Synergy supports the Objection. Accordingly, this Court has subject matter jurisdiction over this matter pursuant to 28 U.S.C. § 157(b)(1), as a core proceeding defined under 28 U.S.C. §§ 157(b)(2)(B) & (K). See also 11 U.S.C. § 1334.

Procedural History and Statement of Fact

Synergy commenced this case on June 4, 2012 by requesting relief under Chapter 11 of the United States Bankruptcy Code.[1] Synergy filed a plan of reorganization and a disclosure statement on April 9, 2013. Talon and the Estate objected. At hearings conducted on June 21, 2013 and July 12, 2013, Synergy indicated that the three parties would come together in an attempt to resolve their differences, but if no resolution was forthcoming, Synergy would file the appropriate pleadings to commence an adversary proceeding for the purpose of determining the extent, validity, and priority of the creditors' respective security interests.

The parties reached no accord, and Synergy initiated its adversary proceedings on July 26, 2013, naming both Talon and the Estate as defendants. Talon and the Estate submitted their answers in response. The docket indicates, however, no additional progress. Subsequently, the Estate filed the Objection before the Court. The Estate contends that it

[1] 11 U.S.C. § 101 *et. seq*.

intended not to supersede the adversary, but to streamline it. The Estate believes that the Court can resolve the primary issues by means of this Objection, leaving only a matter of valuating the collateral in the adversary proceeding.

On notice to all parties in interest, the Court held a hearing with regards to the Estate's Objection on January 17, 2014. Present at the hearing were counsel for Synergy, Talon, and the Estate. After permitting the parties to present their respective positions, the Court asked counsel to submit letter briefs for its further consideration and took the matter under advisement.

Synergy owns real property consisting of a mini-warehouse complex occupying 11.146 acres located at 220 West Highway 34, Newnan, Georgia (hereinafter the "Collateral"). By virtue of an ostensibly perfected security deed, Talon holds a first position lien upon the Collateral. Talon received this security interest by assignment from the Bank of Coweta.

Talon also received by assignment from the Bank of Coweta an entirely separate loan, whereby a corporation known as Property Solutions Group, Inc[2] (hereinafter "Property Solutions") borrowed money and granted a first position security interest in real property located at 5540 Highway 29, Grantville, Georgia (hereinafter the "Property Solutions Collateral"). Talon foreclosed on the Property Solutions Collateral, and the foreclosure resulted in a deficiency in the amount of $521,847.34 that Talon contends should be tacked onto the amount owed by Synergy and subject to its first priority security interest in

[2] The principals of Property Solutions Group, Inc. are the same persons as the principals of Synergy Investment Group, LLC.

Synergy's Collateral.

Respective Party Positions.

Synergy executed a note in favor of Bank of Coweta secured by a Deed to Secure Debt (hereinafter the "Deed"). In addition to identifying the Collateral as security for the loan, the Deed contains an open-end "dragnet" clause that provides:

> This deed is made and intended to secure the payment of the indebtedness of [Synergy] to Grantee evidenced by the Note in accordance with the terms thereof, together with any and all other indebtedness or liability of any nature, whether direct or indirect, absolute, contingent or otherwise, now owing or which may hereafter be owing by [Synergy] to Grantee, however and whenever incurred, whether as principal, maker, endorser, guarantor, indemnitor, surety or otherwise, whether individually and separately or jointly with others (and whether or not such others are parties hereto), and all renewals, extensions or modifications of the Note or other indebtedness, either in whole or in part (all of which are collectively referred to herein as the "Secured Indebtedness").

Movant's Letter Br. Ex. 1. The dragnet clause extends the Deed to cover any additional indebtedness of Synergy to the grantee. Talon concedes that the Deed's language, alone, would not impose the Property Solutions deficiency onto Synergy's collateral. However, Talon insists that specific language in the Synergy Note brings the Property Solutions deficiency within the purview of the dragnet clause, or otherwise the Deed in general. Talon directs the Court to the "Additional Terms" section on page 1 of the Synergy note, which states:

> THIS LOAN IS SECURED BY DSD [(DEED TO SECURE DEBT)] DATED 3/16/06, DSD DTD 10/31/02 MODIFIED 2/17/05, DSD DTD 7/31/02 SECURING MINI WAREHOUSES ON 11.146 ACRES LOCATED @ 220 W. HWY 34, NEWNAN, GA 30263
> DSD DATED 3/25/05 MODIFIED 9/15/05 SECURING LAND LOTS 245 & 246 OF THE SECOND LAND DIST., COWETA COUNTY TRACT B CONTAINING 19.734

ACRES AND TRACT C CONTAINING 5 ACRES I/N/O PROPERTY SOLUTIONS GROUP, INC.
CROSS COLLATERALIZED WITH LOAN #61205619-15.

Movant's Letter Br. Ex. 2. The first paragraph refers to Synergy's Deed. The second paragraph presumably alludes to the Property Solutions Deed.[3] The third paragraph identifies by loan number the Property Solutions note. Synergy executed no other documents. Talon contends that it is clear that the parties intended that Synergy's loan and Property Solutions' loan be cross-collateralized. Talon further insists that the Deed incorporated the entirety of the Synergy note, including this provision, and asks the Court to give favor to the plain, unambiguous language and intent that Synergy pledged the Collateral as security for Property Solutions' indebtedness.

The Estate contends that the cross-collateralization language insufficiently attempted to constitute a third-party pledge or hypothecation agreement, an agreement whereby Synergy would not be directly liable for the debt(s) of Property Solutions, but that the Collateral would be pledged as security for Property Solutions' loan.

Conclusions of Law

A valid "hypothecation[4] agreement," like a guarantee, "create[s] an obligation . . . sufficient to permit the operation of a dragnet clause in the deed to secure debt," so long

[3] The first and second, for lack of better characterization, "paragraphs" appear to identify what collateral secures or ought to secure the Synergy loan, and Talon does not assert otherwise. It is the third "paragraph" that Talon contends causes the Synergy Deed additionally to secure the Property Solutions note.

[4] "The Georgia Supreme Court has recognized that 'hypothecate' means to pledge property in order to borrow money or as security for a loan." Club Assoc. v. Consolidated Captial Realty Investors (In re Club Associates), 951 F.2d 1223, 1231 (11th Cir. 1992).

as the parties to the hypothecation agreement were the original parties to the security instrument. Fleming v. First Am. Bank & Trust Co., 171 Ga.App. 295 (Ga.App. 1984); see also Citizens & S. DeKalb Bank v. Hicks, 232 Ga. 244, 245 (Ga. 1974) ("[T]he guarantee itself was a personal obligation . . . between the original grantor and grantee in the deeds to secure debt. Such personal guarantee created a debt or obligation which could be tacked onto the original deed [by operation of an] open end or dragnet clause[.]"); Citizens and S. Nat. Bank v. Gilbert, 130 Ga.App. 219 (Ga.App. 1973). The facts in Fleming are acutely similar to those before the Court, with the sole exception that no one contested the legitimacy of the hypothecation agreement.

In Fleming, a deed conveying title to property was executed by the appellant and her husband so that the bank would loan money to a corporation in which the husband owned an interest. Fleming, 171 Ga.App. at 295. The deed contained a dragnet clause. Id. Subsequently, the Appellant entered into a hypothecation agreement, authorizing a successor corporation to use the deed as collateral for a loan from the same bank. Id. The second corporation defaulted on the debt, and the bank foreclosed on the appellant's residence. Id. Appellant brought suit for damages, alleging the bank had no right to foreclose on the property. Appellant's primary argument was that there was "no such identity of parties with regard to the loans to the second corporation and that the dragnet clause of the security deed was, therefore, not effective." Id. The Georgia Court of Appeals upheld the trial court's ruling that the foreclosure was proper. Id. The appellate court found that although the appellant had no personal liability for the debt of the second corporation,

the hypothecation agreement subjected the property to additional obligations of the appellant sufficient to bring the second loan into the confines of the dragnet clause's provisions. Id.

The question turns, then, to whether the language—"Cross Collateralized with Loan #61205619-15"—validly pledges Synergy's property for the debts of Property Solutions, so that the dragnet clause—or other provision within the Deed—operates to attach Property Solution's deficiency as an obligation secured by Synergy's allegedly pledged Collateral. An agreement to answer for the debt or default of a third party falls within the statute of frauds, and its effectiveness requires such a pledge to be in writing and endorsed by the promisor or a lawfully authorized agent. See Official Code of Georgia Annotated (hereinafter "O.C.G.A.") § 13-5-30(2).[5] This provision is commonly known as the "suretyship provision" of the statute of frauds. See Restatement (Third) of Suretyship & Guaranty § 11, Comment(a) (1996).

Although the suretyship provision typically governs traditional guarantees, see id. § 11 (using personal guarantees as examples), the Court believes its precepts extend to

[5] A common exception to O.C.G.A. § 13-5-30(2), known as the "original undertaking" exception, appears not to apply in these circumstances. "The difference between a guarantee, which must be in writing, and an original undertaking, which need not be, depends on whether the guarantor is to be primarily liable for the debt. . . . In the case of an original undertaking, . . . the new promisor must substitute himself as the primary party to perform. . . . In other words, . . . the creditor must be looking primarily to the guarantor for complete payment, rather than looking primarily to the third party (and only to the guarantor upon default)." Albee v. Krasnoff, 255 Ga.App. 738, 742 (Ga.App. 2002). In this case, Talon looked at Property Solutions for all payments on its secured obligations and only turned to Synergy upon default. Thus, this exception to O.C.G.A. § 13-5-30(2) is inapplicable.

hypothecation agreements. Cf. Schiska v. Schramm, 1 Or. 647, 652-53 (Or. 1935) (*en banc*) ("It is true that defendant Cox was not personally bound; but that is not essential to create the relationship of surety. . . . Some law writers treat the property pledged by its owner to answer for the debt or default of another as occupying the position of a surety.") (citations omitted); MDL Med. Diagnosis Lab. v. Schram, 2011 WL 2803479, at *4 (Cal.App. 2011) ("A surety or guarantor is one who promises to answer for the debt, default, or miscarriage of another, or hypothecates property as security therefor.") (quoting CAL. CIV. CODE § 2787) (internal quotations omitted) (partially overturned on alternative grounds); Borne v. Grande, 1998 WL 27242, at *1-*2 (Minn.App. 1996) (suggesting that the collateral pledge of an individual's partnership assets on behalf of the debt of her boyfriend would have fallen within the suretyship provision of the statute of frauds, but for a finding that the promise invoked the primary promise exception to the suretyship provision, whereby the promisor makes the pledge primarily to promote his or her own interests); Pearl v. General Motors Acceptance Corp., 13 Cal.App.4th 1023, 1028 (Cal.App. 1993) ("Since under the pledge agreement Pearl 'hypothecated,' or pledged, his stock as security for the debts of Palomar, . . . Pearl is a 'guarantor' and the pledge agreement is implicitly a 'guaranty' for purposes of the suretyship provisions of the Civil Code . . . ."); Smith v. Independence Bank, 119 Wis.2d 900, at *4-*5 (Wis.App. 1984) (suggesting the pledge of securities would have been governed by the statute of frauds, except for a finding that the pledge was for the primary purpose of promoting the pledgor's own interests); First Nat. Bank v. LaFayette Trust Co., 85 Misc. 341, 343 (N.Y.Sup. 1914) (recognizing that if a third party's collateral

was pledged in an oral agreement to answer for the debt of another, it would come under the statute of frauds, as well as the statute's applicable exceptions). Supportingly, the Fleming Court found guarantees and hypothecations interchangeably analogous and held that the hypothecation "created an obligation" in the promisor to have her property answer for the default of another. Fleming v. First Am. Bank & Trust Co., 171 Ga.App. 295, 295 (Ga.App. 1984). Accordingly, the statute of frauds should apply. Moreover, because of the emphasis placed on their similar purpose and function, the Court finds it appropriate that hypothecations meet the general standards required for guarantees in Georgia.

The statute of frauds' requirement that the enforceability of a promise to answer for another's debt hinges on the promise's being memorialized in writing and signed by the promisor "has been interpreted to mandate further that a guarantee identify the debt, the principal debtor, the promisor, and the promisee." Tampa Inv. Grp., Inc. v Branch Banking and Trust Co., Inc., 290 Ga. 724, 728 (Ga. 2012) (citations omitted); Brzowski v. Quantum National Bank, 311 Ga.App. 769, 771 (Ga.App. 2012) (citations omitted). Moreover, the Georgia courts require "that a guarantee must, either in itself or in connection with other writings, identify the debt which is the subject of the promise, indicate knowledge of both the amount promised to be paid and the time the debt becomes due." Tampa Inv. Grp., Inc., 290 Ga. at 728 (citations omitted) (internal quotations omitted); Brzowski, 331 Ga.App. at 771 (citations omitted) (internal quotations omitted).

Clearly, the Synergy note fails to fulfill the criteria specified above. The Synergy note lists the borrower as Synergy and makes no reference to promisors/pledgors or

promisees/pledgees, an alternative principal debt or debtor, alternative amounts to be paid, or an alternative date when the supposed debt becomes due. The question becomes whether the Synergy note incorporates the requisite information by referencing the Property Solutions loan in the "Additional Terms" section. However, it appears that the Property Solutions note also fails to satisfy the statute of frauds requirements. Even assuming that the Court stretches its consolidated scrutiny[6] of the two documents as providing for the principal debtor as Property Solutions and the principal debt, amount to be paid, and due date[7] as listed respectfully on the Property Solutions note, the Court is of the view that at no point do either of the documents identify Synergy as a promisor or indicate knowledge that Synergy promises, pledges, or otherwise hypothecates its property as security for another loan by means of Synergy's loan transaction.

One of the principal statutory purposes of requiring a qualified writing, as evident in this proceeding, is that the "natural formalities that often attend an extension of credit are unlikely to provide reliable evidence of the existence and terms of the secondary obligor's undertaking." Restatement (Third) of Suretyship & Guaranty § 11, Comment(b) (1996).

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[6] "[A] court must strictly construe an alleged guaranty contract in favor of the guarantor. The guarantor's liability may not be extended by implication or interpretation . . . . Thus, this Court is not authorized to determine the identity of the principle debtor, of the promisee, or of the promisor by inference . . . ." See Thompson v. LaFarge Bldg. Materials, Inc., 323 Ga.App. 276, 279 (Ga.App. 2013).

[7] In a side argument, the Estate contended that the Property Solutions note is dated after the Synergy note and necessitates a prospective third-party pledge to accomplish Talon's contemplated theory. The Court, however, acknowledges that the Property Solutions note—presented for its review—constitutes a renewal, and that more than likely, another note, bearing the same loan number, pre-existed the Synergy note's own renewal.

The cryptic reference to cross-collateralization in the Synergy note reveals the desired outcome, and as counsel for the Estate pointed out, that outcome could have been accomplished in a number of ways, including co-signed notes, guarantees, or valid hypothecations. Nevertheless, the truth of the matter before the Court is that Talon, or its predecessor, failed to acquire the same.

Certainly, Talon will assert that the Court declines to respect the intentions of the parties. It is true that the "cardinal rule" of contract construction has long been to "ascertain the intention of the parties[,]" but only so long as the intention is "clear" and "contravenes no rule of law." Skinner v. Bearden, 77 Ga.App. 325, 326 (Ga.App. 1948). The enforceable nature of a contract pledging property for the debt of a third party is governed by the statute of frauds's suretyship provision, which has its roots in old English common law and has been codified in Georgia. See Restatement (Third) of Suretyship & Guaranty § 11, Comment(a) (1996); see also O.C.G.A. § 13-5-30(2). Having failed to satisfy the statute of frauds, giving effect to the intention of the parties would undoubtedly violate a long established rule of law. See Thompson v. LaFarge Bldg. Materials, Inc., 323 Ga.App. 276, 279 (Ga.App. 2013) ("Even where the intent of the parties is manifestly obvious, where any of these [requirements] is omitted from the document, the agreement is not enforceable because it fails to satisfy the Statute of Frauds.").

Conclusion

Having reviewed and considered the integral documents, the arguments of counsel, and the pleadings, the Court finds that to the extent that Talon's claims accounts

for the Property Solutions deficiency, it is unenforceable and shall be disallowed.

Accordingly,

The Estate's Objection to Proof of Claim of Talon DN Investments I, LLC, Claim Number 6-2, is **SUSTAINED**, and Claim Number 6-2 is DISALLOWED to the extent of $521,847.34, representing the amount of deficiency resulting from the foreclosure of the Property Solutions Collateral.

The Clerk is **DIRECTED** to serve a copy of this Order on Synergy, the Estate, Talon, respective counsel, and the United States Trustee.

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